Folder Title: Contacts with member countries: Zambia - Correspondence 01

Folder ID: 1771246

ISAD(G) Reference Code: WB IBRD/IDA 03 EXC-10-4549S

Series: Contacts - Member Countries files

Sub-Fonds: Records of President Robert S. McNamara

Fonds: Records of the Office of the President

Digitized: June 28, 2013

McNamara Papers

Contacts
Zambia (1968-1978)

ZAMBIA

ZAMBIA

1.	4/29/68	E. Mudenda, Minister of Finance (see attached attendance list)
2.	5/16/69	Mark Choma, Personal Assistant to the President of Zambia Ambassador Rupiah B. Banda
3.	9/30/69	Elijah Mudenda, Minister of Finance E.G. Kasonde, Permanent Secretary, Ministry of Finance and Development
	9/28/71	Elijah H.K. Mudenda, Minister of Foreign Affairs (with delegation from Organization for African Unity -- Memo filed Mauritania)
4.	Visit 11/15-18/72	RMcN Impressions (Filed in SMcN office) " Notes of Meeting with Pres. Kaunda
5.	"	Memo: Discussions with Ministers and Officials in Zambia during Mr. McNamara's Visit November 15-18, 1972 (Dean) Mr. Mainza Chona, Vice President and Minister of Development John M. Mwanakatwe, Minister of Finance Reuben C. Kamanga, Minister of Rural Development Wesley P. Nyirenda, Minister of Education Fwanyanga M. Mulikita, Minister of Power, Transport and Works Humphrey Mulemba, Minister of Mines Solomon Kalulu, Minister of Lands and Natural Resources Ackson Jasper Soko, Minister of Trade and Industry
6.	4/19/75	President Kaunda
7.	5/19/78	President Kaunda - Breakfast at Blair House (alone)

FORM NO. 57

INTERNATIONAL DEVELOPMENT ASSOCIATION | INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: Files

DATE: May 1, 1968

FROM: S. Noel McIvor

SUBJECT: Zambia

The Minister of Finance of Zambia, Mr. Mudenda, called on Mr. McNamara on April 29. Also present were the Zambia Ambassador; Mr. Kasonde, Permanent Secretary of the Ministry of Finance,of Zambia; and Messrs. Knapp, Shoaib, Coleman and McIvor.

There was the usual exchange of courtesies. Mr. McNamara then asked the Minister about the Tan-Zam Railway and the Minister said that having failed to secure serious interest elsewhere, they had agreed to the Chinese offer to engineer the Railway. Asked about the recent Government announcement that 51 per cent of 25 businesses was being taken over, the Minister said that this had been the Government's reply to profiteering by foreign firms in Zambia. He thought that a substantial Government interest in a number of firms would stimulate competition and reduce prices.

The Minister then said that he wished to speak to Mr. McNamara alone on some matter which was not Bank business. He and the Ambassador then remained with Mr. McNamara and the rest of the group withdrew.

Biographical Note on the Hon. Elijah Mudenda

The Hon. Elijah Mudenda, Minister of Finance, was born in the southern province of Zambia in 1927. He was educated in Zambia, Uganda, South Africa and Cambridge, England, where he graduated as an agriculturalist. He worked for the government until 1962 as an agricultural research officer in plant breeding.

In 1962 he was appointed Parliamentary Secretary to the Ministry of African Agriculture in Northern Rhodesia's first African government, and after the 1964 elections he became Minister of Agriculture. In the United National Independence Party elections in 1967 he stood for the post of party treasurer against the then Minister of Finance, Arthur Wina. He won the election, and was subsequently appointed Minister of Finance.

Africa Department,
April 26, 1968

LIST OF OFFICIALS ACCOMPANYING
THE MINISTER OF FINANCE OF ZAMBIA

(1)	Mr. E.G. Kasonde	-	Permanent Secretary, Ministry of Finance
(2)	Mr.M.C. Chona	-	Special Assistant to the President
(3)	Mr. S. Masiye	-	Permanent Secretary, Office of the President
(4)	Mr. C. Linyama	-	Economist, Office of National Development and Planning
(5)	Mr. Matyola	-	Administrative Officer

Mr McNamara - to see, please.

FORM NO. 57 INTERNATIONAL DEVELOPMENT ASSOCIATION | INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | INTERNATIONAL FINANCE CORPORATION

RMSS 5/20

OFFICE MEMORANDUM

TO: The Records

DATE: May 19, 1969

FROM: A. G. El Emary

SUBJECT: Zambia - Western Railroad

Mr. Banda, the Zambian Ambassador, Mr. Mark Chona, Special Assistant to the President of Zambia, and Mr. Musukwa, First Secretary at the Embassy of Zambia, visited Mr. Mc Namara on Friday, May 16. Mr. Aldewereld and Mr. El Emary were present.

Mr. Chona said that his President asked him to express to Mr. Mc Namara how pleased he was that the relations between Zambia and the Bank had lately improved and that the mutual trust had been manifest. He then referred to the letter, addressed to Mr. Mc Namara by the President of Zambia, which he brought with him. Mr. Mc Namara said that he had seen it, but he was surprised to see in it a statement attributed to Mr. Knapp concerning the Bank's favorable disposition towards a proposal to construct a railway line linking Zambia directly with the Benguela Railway in Angola. The fact of the matter is that Mr. Knapp expressed serious doubt whether the Bank would consider it even if it were presented officially by Zambia.

Mr. El Emary read Mr. Knapp's statement from the minutes of the meeting held in the Bank on September 13, 1968 between Mr. Knapp and representatives of American Metals Climax Corporation and Roan Selection Trust: "Mr. Knapp said that, as they would expect, he could not give any answer to whether, if and when such a project were developed, the Bank would be willing to consider it. He stressed the delicate position of any project which involved Portugal, South Africa or Rhodesia, as a result of U.N. criticism. ..."

On hearing this, Mr. Chona expressed relief. He said that they were given a wrong impression of the Bank's attitude. He said that the same erroneous information was published in the Johannesburg Star and in Lisbon, and in addition it was mentioned that Zambia was about to conclude an agreement with the Benguela Railway to construct the link between Zambia Railway and the Angola lines. He added that Zambia, being a landlocked country, would benefit from the opening of additional routes, but at present Zambia could not avail itself of the link with the Benguela lines. The main obstacle is the status of Angola as a Portuguese colony. In any case, he said that Zambia was going ahead with Tan-Zam Railway and it did not seem likely that Zambia could get involved in the finances of both links, one to the East and the other to the West, at the same time.

Mr. Mc Namara said that the Bank would not consider the western line project unless it was requested officially by Zambia and that Zambia expressed its interest in the project in the open.

Mr. Chona expressed his satisfaction with Mr. Mc Namara's statement by thanking him.

President has seen

Mr. Chona then turned to his other purpose for the visit. He said that President Kaunda hopes that Mr. Mc Namara would be able in the near future to visit Zambia. To that, Mr. Mc Namara replied that as soon as time permitted he would suggest some date for his visit that would meet the convenience of the Zambian Government. He said that he was eager to visit Zambia and asked Mr. Chona to thank, on his behalf, President Kaunda for his invitation.

cc: Messrs. Knapp/Cope
Aldewereld
Chadenet/Baum
Sadove
Kruithof

AGElEmary/fob

Mr. McNamara - to see, please.

FORM No. 57

INTERNATIONAL DEVELOPMENT ASSOCIATION | INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | INTERNATIONAL FINANCE CORPORATION

RBS 5/13

OFFICE MEMORANDUM

TO: Files

DATE: May 13, 1969

FROM: J. Burke Knapp JBK

SUBJECT: Zambia

Fri 5/16

I received a telephone call yesterday afternoon from the Zambian Ambassador, who said he had just returned from Lusaka bearing a message from President Kaunda as follows.

Kaunda would like to send his personal assistant, Mr. Mark Choma, to Washington "as soon as possible" to discuss with the Bank the full range of "Zambia's railway problems". Mr. Choma would be ready to come on a day's notice and would like to see Mr. McNamara and myself. In response to my question, the Ambassador said that he would like to discuss with us the TanZam railway and the "railway to the West". (This is the copper company's proposal to construct a new rail link connecting with the existing Benguela railway to the port of Lobito in Angola.)

After checking Mr. McNamara's schedule and after talking with Messrs. El Emary, Aldewereld and Baum, I called the Ambassador back last night to say that we would be glad to receive Mr. Choma on Friday of this week. I explained that I would not be available but that Mr. El Emary would receive Mr. Choma and that Mr. McNamara and Mr. Aldewereld would be available to see him. The Ambassador is to notify Mr. El Emary of Mr. Choma's traveling plans.

cc: Messrs. McNamara, Aldewereld, El Emary, Cope,
Baum, Sadove

President has seen

[illegible]

FORM NO. 57 INTERNATIONAL DEVELOPMENT ASSOCIATION | INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: The Record **DATE:** October 15, 1969

FROM: A. Kruithof *dw 16*

SUBJECT: Zambian Delegation Meeting with Mr. McNamara
Annual Meeting 1969

1. On Tuesday, September 30, 1969 The Honorable Elijah Mudenda, Minister of Finance from Zambia, accompanied by Dr. J.B. Zulu, Governor of the Bank of Zambia, and Mr. E.G. Kasonde, Permanent Secretary, Ministry of Finance and Development, called on Mr. McNamara at the Sheraton Park Hotel. Also present for the Bank were Messrs. Knapp, El Emary, Brakel and Kruithof.

2. The Minister expressed appreciation for the Bank's assistance to - and interest in - Zambia and mentioned in particular the noticeable improvement in relations during the last few years. He would like later to set forward Zambia's views on the Bank's interest rates for projects in education and agriculture. The Minister felt strongly that those rates should be lower than 7%; he thought that Zambia should qualify for IDA funds for these projects or alternatively there should be a "subsidized" interest rate for them. Mr. McNamara agreed with the Minister that interest rates are high but this is a worldwide feature and all he and his staff could do under current circumstances was to try to avoid a further increase in the Bank's rate.

3. The Minister also mentioned that the Bank's requirements in respect of international bidding were sometimes conflicting with Zambia's policy of promoting local contractors. He was leaving this subject for Mr. Kasonde to discuss during forthcoming negotiations. (Note: The conflict concerns only civil works contracts below a $140,000 contract price. Such contracts are not likely to be used in Bank financed projects and in the Education loans (past and proposed) they are to be awarded on the basis of domestic competitive bidding only.)

4. The Minister reported that the discussions with the mining companies on the takeover of a 51% share by the Government were progressing satisfactorily and in a good, amicable spirit. No major difficulties are foreseen. He volunteered that the Bank, being a major creditor of Zambia, was entitled to be brought into the picture of these developments. He pointed out in particular the advantages of the Government acquiring the mineral rights. This had already resulted in an interest from other countries like Japan and the U.S. in possible mining ventures.

5. Mr. McNamara said that we would follow further developments with great interest, especially the Government's efforts to expand the mining industry and the expected increased exports resulting therefrom.

AKruithof:jk
cc:Messrs. McNamara, Knapp, El Emary, Brakel

RMcN Chron

NOTES OF MEETING WITH PRESIDENT KAUNDA OF ZAMBIA

November 16, 1972

1. I stated:

a. The relationships between Zambia and the Bank in the past had not been satisfactory for either party: Zambia felt the Bank did not come to its aid immediately after UDI; and in the late 1960s when copper prices were high and when Zambia did not wish to accept Bank assistance, the Bank failed to emphasize that the nation should then be planning for the longer term when copper prices would be lower and external capital requirements high. I added it was my hope, and one I knew he shared, that our relations in the future, particularly in the fields of agriculture and education, could be much closer indeed.

b. The development plan was well conceived but totally unrealistic in its relationship to available funds. It was essential that the investment program be cut and that current expenditures be squeezed as well.

c. If they would prune the program and develop a realistic financial plan, we would re-examine our lending program and do everything possible to increase it, placing particular emphasis on agriculture and education. (I mentioned specifically the weakness of their agricultural education program.)

d. We were very concerned at the delay in the decisions relating to Kariba. (These were causing a loss of almost $2 million per month.) There was need for: a prompt decision regarding the choice of contractor; a full-time Zambian manager of KNBC; and suspension of the provisions of the Mining Act.

e. He and his government have performed miracles since independence, starting as they did with only 100 college graduates and 1000 high school graduates, but it appears that too much reliance has been placed on the use of expatriates, without adequate plans to replace them at the end of a reasonable time.

f. I strongly supported his view that first priority must be given to development of rural areas and for this purpose "Intensive Development Zones" was an excellent concept, but I could find no substance behind the plan.

2. During the conversation, Kaunda stated:

a. Prior to the McNamara regime, relations with the Bank were very strained.

b. At the time of independence the nation started with: frictions between blacks and whites; only 100 college graduates; a modern sector limited to the "line of rail" and a deprived rural area; the penalties and frictions of UDI; a land-locked country whose exports literally passed through enemy territory.

c. His government is trying to maintain both political democracy and economic democracy.

d. One of their biggest problems at the moment is the movement to the cities from the rural areas.

e. The development of Zambia in Southern Africa, surrounded as it is by apartheid-oriented regimes, is a very serious problem. It is terrifying that people (that is, the Western Powers) professing Christianity (his faith) should support countries like Portugal, Spain, and Rhodesia. Why do we allow the Communist countries to take advantage of this? It is only the big countries of the West that can now help solve this problem -- if they don't do so, a racial war is inevitable.

Robert S. McNamara

OFFICE MEMORANDUM

TO: Memorandum for the Record

DATE: December 14, 1972

FROM: Robert M. Dean RMD.

SUBJECT: Zambia: Discussions with Ministers and Officials in Zambia during Mr. McNamara's Visit November 15 - 18, 1972

Accompanying Mr. McNamara were Messrs. Ismael El Misbah Mekki, Alternate Executive Director for Zambia; S. Shahid Husain, Program Director, East Africa Region; Robert M. Dean, Program Division Chief, East Africa Region; Anders E.E. Ljungh, Personal Assistant to the President, and on occasion William Clark, Director, Information & Public Affairs Department.

The following meetings were held:

Vice President's Office

Those present included the Vice President and Minister of Development Planning, Mr. Chona and the Ministers of Finance, Mr. Mwanakatwe; Rural Development, Mr. Kamanga; Education & Culture, Mr. Nyirenda; Power, Transport & Works, Mr. Mulikita; Mines, Mr. Mulemba; Lands & Natural Resources, Mr. Kalulu; Trade & Industry, Mr. Soko.

The Vice President said that the government was unhappy that so far Zambia had not been allocated any IDA funds. He understood that national income on a per capita basis was the criterion used by the Bank to determine whether a country was eligible for IDA funds. In the case of Zambia, the national income fluctuates considerably, because about 40% comes from copper, the income from which goes mainly abroad. Therefore, in his view, the criterion was not a good one. He also suggested that the current liquidity crisis was a justification for IDA being considered for Zambia, and he suggested further that certain projects, such as Site & Service schemes to assist in their urban squatter problems and urban water supply and sewerage schemes, were particularly suitable for IDA lending.

Mr. McNamara replied that IDA funds were limited by the amount which we were able to raise from Part I countries. Its total was much less than the financing needs of even the most poor countries. As a result, the four largest Part II member countries, India, Pakistan, Indonesia and Bangladesh with a combined population total of 820 million get an annual total of IDA equivalent to about 80 cents per capita per year. This was a patently inadequate level of financial assistance to these countries, which did not have in relative terms even those advantages with which Zambia was blessed, such as mineral resources which were being exploited on a considerable and efficient scale. They were not creditworthy for Bank loans and therefore it was imperative to give them a maximum allocation possible of limited IDA funds. On the same

President has seen

per capita basis, Zambia, with her population of about 4 million, would get \$3.2 million of IDA funds. The Vice President said that just as his government was motivated by the philosophy of humanism in Zambia, which stresses the dignity of every person he completely accepted the prior need for IDA funds of the peoples of India, Pakistan, Indonesia and Bangladesh. He said he did not accept the second argument that an allocation of IDA to Zambia on the same per capita basis would not be worth while; such an amount would be a useful though small contribution to her current financial needs.

The Vice President then went on to outline the government's economic strategy which was to give priority to rural development. In this sector they had in this current plan two main objectives. The first was to attain self-sufficiency in food production; the second was to make a substantial beginning to the move from what he called traditional to progressive rural communities. The government's policy in the industrial sector was one of diversification and they wanted particularly to stimulate the production of materials and equipment for the mining industry and agriculture. As far as education and training were concerned, their main immediate aim was to reduce their dependence on expatriate skills.

The Zambian government welcomed increased Bank participation in their projects, especially due to the current financial stringency and they would like us to move into more directly productive fields, such as intensive development zones and industrial projects.

Dealing with the current financial difficulties, the Vice President said that the floating of the Pound Sterling (which has been downwards against the Dollar to which the Kwacha is linked) and inflation in developed countries from which Zambia's imports are drawn, have both increased the difficulties resulting from the drop in copper prices and the substantial fall in production due to the Mufulira disaster. The Vice President said the government intended to cut expenditures but also thought that they must increase foreign borrowing.

The Vice President said that he would like to conclude by mentioning the important fact that Zambia's difficulties were considerably increased by her geographical position: she is a land-locked country surrounded by four independent and four non-self-governing countries. There is a great deal of tension on some Zambian borders and goods in transit to and from Zambia passed through the territories of hostile regimes who on occasion use this power to blackmail Zambia.

Mr. McNamara asked what is the expected trend of food imports and what problems are seen in the plans to achieve self-sufficiency in food production.

Mr. Kamanga said that half the beef consumed in Zambia was provided internally and half by imports. The traditional attitude to cattle as a store of wealth rather than source of regular income inhibited a greater off-take of cattle for slaughter. Changing these traditional attitudes would take a long time, so that the government has in the meantime set up State ranches and has increased beef prices to attract producers. The government was hopeful that production of pork would increase on the basis of the recent encouraging trend. He mentioned that there was almost no production of wheat in Zambia; it would need irrigation. There had been a good response in the villages to production of oil seeds which was being encouraged. The government was also distributing fruit trees to farmers from its nurseries in an effort to encourage fruit production; fruit currently is almost entirely imported. The Vice President said that the rural development program was intended to try and halt the drift to towns, which appeared very attractive compared with the situation before Independence when, due to racial discrimination, it was not comfortable for an African to live in town. The government's aim was to make rural living as attractive as urban living.

Mr. Mwanakatwe said that he would like to ask Mr. McNamara whether there was any possibility of help from the Bank for their current problem which left them with the shortage of resources needed to finance the local costs component of projects; in particular he asked whether there was any possibility of a program loan from the Bank.

He explained that the Articles of Agreement of the Bank require that such lending only be done in exceptional cases. He said that the Bank's Board has been more willing in recent years to make "exceptional" local cost lending. He said that in the case of program loans, which were also possible under the Articles of Agreement, the circumstances have to be even more exceptional than those which justify local cost lending, so that the possibilities for program loans are very limited. Mr. McNamara explained that there was a number of prerequisites to local cost financing on any scale or a program loan among which is that there is a prudent and balanced financial plan developed in the light of the current financial situation. Because the Bank's Board was much more reluctant to contemplate program loans, mainly because it was not easy to identify the results of such lending, it would be necessary to show that there was some unusual circumstance attaching to the situation, such as the recent Mufulira disaster which resulted in an unforeseen and substantial loss of copper production and that the government had developed an appropriate investment and financing plan to deal with circumstances.

Mr. Nyirenda said that in the area of his responsibility - education - the Bank's implementation procedures had been too slow. Much time had been spent on sending vast amounts of detailed worksheets and plans to Washington; moreover, the Bank staff had been inflexible and unresponsive to local views. He gave as an example a long standing difference of opinion on the appropriate ratio of day pupils to boarders in secondary schools in the rural areas. He was concerned that the Bank worked on wrong data which it was unwilling to recognize.

Mr. McNamara said that he was concerned to hear the Minister's complaints. He explained that the World Bank belongs to its members; thus Bank staff, including the President, were hired by the countries to work as professionals on their behalf. We make judgments on the facts available to us to the best of our professional ability. Officials in the Ministries and officials in the country may differ about judgments and he hoped that such differences could be discussed in good faith and with respect on both sides. If nevertheless differences remain they should be recognized before any financing is approved and not submerged only to emerge later during implementation of the project. If it is impossible to reach agreement, this should be frankly recognized and the Bank should move on to some other area in which agreement on the basis for financing can be reached.

The Vice President asked the Acting Permanent Secretary of Ministry of Local Government, in the absence of the Minister, to describe the government's plans for low cost housing development, explaining that the government's wish is to foster the traditional Zambian practice of a family owning his own home. Mr. Mabukwanu said that the government calculated that there was a need for a 140,000 sites for low cost housing to be constructed as "site and service" schemes. The Second National Development Plan makes provision for 70,000 sites of which 63,500 are low cost, which require materials costing between K50 and K2000, in addition to K500 estimated cost for the service plot. The schemes were based on local authority loans and technical assistance to families who would build their own houses on the serviced plots. In addition, the government plans to help local authorities to up-grade "squatter areas", at least those which are selected as being suitable for such up-grading. Piped water and roads would be put in and provision made for refuse removal. At the second stage, water-borne sewerage would be put in. He hoped that the Bank would find it possible to assist in the financing of these programs.

Mr. McNamara said that we have been extremely interested in the report which some consultants had made to the Bank on Zambia's experience of site and service scheme. This was an area in which the Bank was learning and if we could at the same time both learn and help Zambia, we would be most interested in being able to do so. Mr. McNamara said that he would like to find time to see such a scheme in Lusaka. This was arranged. Mr. Kalulu mentioned that the Industrial Forestry project which the Bank had financed was going well and the government hoped that a second one could be developed sooner than originally envisaged and linked with government plans for a wood processing industry.

The Vice President asked if Mr. McNamara had any comments on the effect of Zambia's geographical position on her economic development. Mr. McNamara said that he did not wish to comment on the political aspects of this matter but that clearly very high transport costs were one result which had a significant effect on the economic situation. Mr. McNamara went on to ask if the income gap between the rural and urban areas had widened in recent years. His impression was that it had and if this were correct, he asked what general economic policy the government planned to deal with it, for example were there plans to try to hold down urban wages.

The Vice President said that the previous law setting a limit of 5% in wage increases in a year although no longer the law still virtually applied in practice and the government intended to try to maintain its effect. In addition, they kept/prices which they controlled high to agricultural encourage increased production and increased rural incomes.

Ministry of Education

Those present included the Minister of Education, Mr. Nyirenda; the Vice Chancellor of the University, Dr. Goma; the Permanent Secretary, Mr. Adamson and the Director of the Commission on Technical & Vocational Education, Dr. Ford.

Mr. McNamara asked for some data on the current educational system. Mr. Adamson replied that in the First National Development Plan (1966-71), it was planned that 33% of children in primary schools would go to junior secondary schools (3 years) and 75% of those in the junior part of the secondary schools would progress to the senior part (2 years). In the Second National Development Plan these percentages were revised to 25% and 50% respectively. This year about 21% of primary school leavers will go to secondary schools. He said that well over 90% of 7-year-olds have places in primary schools. The Permanent Secretary said that their big problem was what he calls 7th grade, i.e. primary school leavers, drop-outs and the Ministry was instituting some pilot projects for vocational centres for such children. Mr. Ford said that 2,000 to 3,000 places in technical schools were available for Form 3 (Grade 10) and 3,800 places for Form 5 (Grade 12) leavers.

Mr. McNamara asked why so little agricultural education was available, particularly for primary school leavers. The Minister said that the wrong attitude to practical work still persisted in Zambia. They were trying to counter this by the introduction of agricultural and environmental studies in the primary and secondary school curricula. Mr. McNamara said he thought that there was a need for more training of middle level agricultural technicians, that is those with less than a college level education. If this assumption were correct, it would reduce the problem of employing primary school leavers. Mr. Nyirenda said that the National Resources Development College produces agricultural demonstrators, but he agreed that its output fell far short of needs. Mr. Adamson said that it was planned that the three agricultural colleges would produce enough to meet the need for senior level agricultural manpower. The Minister said that the government was studying the possibility of ten years of primary school because children at 14 were too young for employment. They would want a very diversified curriculum so that when leaving at 17 the students would be fitted for a wide range of employment.

Dr. Goma, the Vice Chancellor, said that 13% to 15% of those writing the school certificate at present go to the University. In 1966, the number was 300, this year it is 1,800 and in 1976 it is estimated it would be 3,000. There are schools of engineering (5 year course), agriculture (4), education (4), humanities (4), social studies (4), law (4), medicine (7), natural sciences (4), mining begins next year (6), a school of nursing is planned. The University attempts to meet the country's needs as far as possible and sets quotas by the school of study. In the first year students are divided into two groups, science and non-science and in the second year go to their special schools. The main need at the moment is for secondary school teachers, especially science (only 14% of secondary teachers at present are Zambians) and secondly for science graduates including agriculture and medicine.

Only 7% of the teachers at the University are Zambians and the Vice Chancellor's big problem is how to mould the staff from so many countries and academic backgrounds together to respond to the needs of Zambia. Both the Vice Chancellor and the Minister said that in the education projects financed by the Bank, the Bank's staff have been unyielding and have put undue pressure on Zambia. They appear to be bound by undisclosed guide lines which Zambia has found very unsatisfactory, for example, criteria for cost and space produced and used by the U.K. University Grants Committee have been used by Bank missions on a selective basis, whereas the Vice Chancellor said that these criteria were developed for use on a comprehensive basis; selective use therefore needs justification, which, he complained, Bank staff had not given.

Mr. McNamara said that he wanted the government to inform Mr. Dean or Mr. Husain or even himself personally of such problems in future. He undertook that we will always be willing to justify the use of any particular standards by Bank staff. If we do not, Zambia should complain. We could discuss and we may differ at times and if it is impossible to reconcile our difference, we should move on to projects on which we can agree. Mr. McNamara said that he would ask Mr. Dean to stay on to go into the details of the complaints. (In the event, neither the Minister nor officials were available and the matter will be taken up in correspondence).

Ministry of Rural Development

Those present included the Minister, Mr. R. Kamanga; the Ministers of State, Messrs. Ng'andu and Vibetti; the Managing Directors of the Tobacco Board, Mr. Lumina; Rural Development Corporation, Mr. Mutale; the Cold Storage Board, the Dairy Produce Board and the National Agricultural Marketing Board.

Mr. Kamanga gave a review of the present agricultural situation and rural development policy. He explained that the bad crop years in 1969 and 1970 had led to subsidies being given to the importation of food which it was now difficult to remove. With higher producer prices, the government was trying to encourage production of oil seeds, sun flowers and ground nuts, beef and tobacco, for which many successful one acre smallholders wanted more land. Last year's production was 13 million pounds and this year it will be 12 million pounds, compared to 24 million pounds for 1964. They had successfully eliminated the import of poultry and eggs and there was some export of day-old chicks. Production of milk had dropped due to the departure of European farmers and large quantities of powdered milk were imported. The Minister said that the government was attempting to redress the imbalance between the urban and rural areas by the policy of higher prices for agricultural products as well as by the expansion of marketing facilities. He mentioned that before Independence the prices in rural areas away from the line-of-rail were lower. Now, fertilizers and seeds are subsidized to a greater extent in remote areas than on the line of rail.

The low density of population in Zambia prevented them from adequately covering all rural areas with the inputs necessary for rural development and so they have developed a policy of concentration in a few selected areas. Eight Intensive Development Zones were planned for the first year of the plan and 23 by the end of the plan, but financial difficulties have forced a cut in these plans to three in the first year (one in the Eastern Province, one in the Northern Province, one in the Northwestern Province). The areas would be carefully selected on the basis of good soils, adequate water and reasonable communications. The government would put in social amenities, such as schools, hospitals or clinics and better roads to try and reduce the relative attraction of towns. The government will encourage and perhaps direct the production of particular crops in particular areas. The concept involved not just the Ministry of Rural Development but other Ministries as well. The selection of actual sites will be made by the Provincial Ministers.

Mr. McNamara asked about the training of extension officers and the reply indicated that there were not enough being trained, though the Minister mentioned that the National Service Scheme run by the Ministry of Defence was largely concerned with agriculture. He also mentioned District Training Centres which give one and two week courses for men and wives from the village. There are also Provincial Training Institutes which give refresher courses for extension workers. The government's credit organization (Agricultural Financial Company) provides loans to farmers only if they are practicing improved methods of agriculture. The officials of the Ministry were unable to give answers to Mr. McNamara's questions relating to the production targets, investment costs, number of families and expected per capita incomes of either the intensive development zones or on a country wide basis.

Ministry of Finance

Those present included the Minister of Finance, Mr. Mwanakatwe; (at the first meeting) the Governor of the Bank of Zambia, Mr. Kuwane and the Secretary of Finance, Mr. Chibwe and the Director of Planning, Mr. Nkuwani.

Two meetings were held with the Minister of Finance and his officials. The first on November 16 which was in the nature of a courtesy call and the second on November 17 for substantive talks. The note covers both meetings. In the first meeting, Mr. McNamara said that he was particularly interested to find out about dualism in the Zambia economy and in understanding more about the relative share of the modern and rural sectors in gross domestic product. He also mentioned the Bank's desire to learn from Zambia's experience with site and service housing schemes which is a new field for the Bank but one into which we wanted to expand as quickly as possible. Another new field Mr. McNamara mentioned was tourism.

Mr. Mwanakatwe said that he was glad that tourism had been mentioned since he felt that the government had neglected the development of this sector in the first seven years of Independence. He said that a U.S. Foundation had taken over the running of one of the Zambian National Parks for a 20 year period. Mr. McNamara said that he thought it should be possible for Zambia to achieve a similar development of tourism as that in Kenya, where it had taken 7-8 years.

At the second meeting, Mr. McNamara asked the Minister of Finance how he planned to deal with the financial situation in relation to the Second National Development Plan (1972-76). Mr. Mwanakatwe said that severe budgetary cuts were made in 1972 and a similar stringency would be applied to 1973 estimates. The government was considering applying to the IMF for a standby credit. It had also discussed with friendly bilateral aid donors the possibility of short-term credits and the possibilities of increased domestic borrowing will be considered.

Mr. Mwanakatwe had visited Canada, Germany, Sweden, United Kingdom, Denmark and Japan in July and August with the purpose of obtaining financial assistance as quickly as possible. Some loans for specific projects were negotiated; for example, a loan for the purchase of railway engines in Canada which will involve disbursements in 1973 of between K30 and K35 million. He said that he had discussed the possibilities of domestic borrowing in some detail with the Fund mission which had just left after Article XIV consultations. He estimated, bearing in mind reasonable limits on inflationary pressure, that a total of K10-K15 million of domestic borrowing could be contemplated. The Minister said that all these measures would not meet the likely gap between resources and expenditures and they had as a priority task for the Ministry of Development Planning and his Ministry to revise the plan for the next two years. This job he estimates would take them 6-8 weeks.

Mr. McNamara said that he felt the government should make a formal request to the IMF for a standby credit immediately. He also considered that, bearing in mind the lead time for projects, it would be necessary for Zambia to prepare a detailed program for two years and a less detailed but still financially clear program for the succeeding years. He stressed that the important assumptions for this planning, such as the level of copper output, the use of power from Kariba South and other power sources in Zambia as well as the copper price need to be carefully reviewed and coordinated. It was Mr. McNamara's impression that narrowing the gap would involve very difficult decisions to determine priorities and that it could not be closed without social, political and economic costs. He said that the budget projections must be based on a realistic estimate of the available resources. These and investment priorities must be worked out and agreed before he would be prepared to present the loan for Kafue II to the Executive Directors.

Mr. Mwanakatwe said that in 1970 the government had decided to freeze wages. It was a hard decision for them to take and succeeded for a year. He had hoped that it would be possible to make it a permanent policy, but it was not so. In 1971 and 1972, a rise took place, not as bad as that prior to 1970 but still bad. Their present policy to deal with this problem involved setting up institutions and procedures for wage bargaining; the necessary Acts of Parliament for this purpose had been passed, and provided that when a deadlock in bargaining exists an Industrial Relations Court would decide; its decision would be binding on all parties. The court is to be established early next year and would be given a guideline of 5% as the annual limit on wage increases.

The Minister asked Mr. McNamara for more information about the possible program loan which he hoped the Bank would consider, and Mr. Chibwe asked how long Mr. McNamara thought it would take to make arrangements for such a program loan. Mr. McNamara replied that if by mid-

January the government had revised financial plans for both recurrent and capital expenditures in detail for 1973/74 and in broader outline for 1975 through 1977, then the Bank would send a mission by the same time as the Fund in late January. He stressed that he would not consider a program loan from the Bank without a standby credit from the Fund. If the work of these missions in Zambia were to be completed by early February, then he thought it would be possible to go to the Board in April. Mr. Mwanakatwe asked if such a loan could be spent "across-the-board", that is for any purpose. Mr. McNamara said not exactly; it would be tied to some category of imports and conditional on an agreed investment program. Mr. Mwanakatwe asked how big the program loan might be. Mr. McNamara said that he preferred not to say it at this stage but he gave some examples: that to India amounted to 15 cents per caput and to Columbia $2.50. Mr. McNamara stressed that this idea of a program loan had not been considered by him before his arrival in Zambia, that it was therefore at a very early stage of consideration in the Bank and that he wanted it be kept very confidential and out of the newspapers. Mr. Nkwani asked how much Bank lending could be expected over the next two to five years for the purposes of the planning. Mr. McNamara again said that the level of Bank lending would be substantially higher than in the past. The problem should be worked at from both ends. It should be built up from the project base, on which the government had information for those projects already discussed between themselves and the Bank staff, and also from the other end by estimation of resources. He advised the government to concentrate on project development, especially in agriculture and IDZ in particular. Mr. Mwanakatwe said that in their current efforts to protect their foreign exchange resources they had placed a monthly limit on imports, both visible and invisible, with the intention of limiting the monthly bill to K27 to K30 million compared with K37 million prior to the imposition of the limits.

Mr. McNamara said he felt, on the basis of what he had been told, that the idea of intensive development zones as a technique for rural development was a good concept, but he had been unable to discover any quantitative substance to these ideas. Without this of course they would mean very little. He also suggested that the Ministry of Power should have a detailed timetable for completion of the arrangements for financing of Kariba North and Kafue II and he had asked Mr. Dean to remain in Zambia to consult with the appropriate officials to agree on such timetables. A timetable for the discussions in connection with the revision of the plan and standby finance would also be discussed by Mr. Dean.

Ministry of Trade & Industry

Those present included the Minister of Trade & Industry, Mr. A.J. Soko; officials of his Ministry and executives of INDECO and INDECO subsidiaries.

The Minister said that the country's industrial policy was to develop industries not only to substitute for imports but also where possible for export. He asked whether the Bank would make loans for industry. Mr. McNamara said that it was perfectly possible for the Bank to make loans for industrial projects. However, he thought that the new program priorities which the Zambian government would work out in the near future, to contend with its financial difficulties, might well involve cuts in the industrial program. Representative of the sugar company said that the industry planned to expand to meet all Zambian requirements by 1976. He said present imports were between 15,000 and 17,000 tons, valued at about K2 million. Consumption was increasing at between 10% and 15% per annum and the capital requirements for the expansion program between 1974 and 1977 totalled K5 million; the present expansion program until 1974 was already financed. Other spokesmen described textile and fertilizer plants which produced at costs of 25% and 33% respectively above import parity prices. There were plans for production of building materials, the import bill for which totalled K27 million in 1971.

Mr. McNamara said that he would be reluctant to consider financing sugar expansion, a product the consumption of which in Zambia was increasing so fast as to warrant the consideration of price and taxation measures to control it. He was more attracted to the idea of production in Zambia of building materials and brassware in which the high transport cost would give the country a comparative advantage. He cautioned the meeting against uneconomic industrial expansion as compared to that based on products in which Zambia's competitive position was good on a long-term basis.

Ministry of Power, Transport & Works

Those present included the Minister, Mr. Mulikita and the Permanent Secretary, Mr. P. Siwo.

Mr. McNamara asked what were the major problems facing the country in the power sector. Mr. Mulikita said that the main aim of the government was to sever its dependence on Rhodesia for electric power. For this reason, Kafue Stage I was built and became operational last April. Kafue II would make a major addition to the capacity of the scheme and together with output from Kariba North and other Zambian schemes make the country independent of Rhodesian supply.

Mr. McNamara asked for an account of the present situation on Kariba North and was told by the Minister that the government was waiting for advice from the consulting engineer, Sir Alexander Gibb & Partners, as to whether the present contractor should be allowed to continue or should be removed from the site. He said that the government was anxious to take such decision as quickly as possible because of the enormous cost of delay. Mr. McNamara said he appreciated the care with which Gibb would have to prepare such opinion, but he considered that they should be able to give the government a date by which such an opinion should be available. Mr. McNamara also urged on the Minister the necessity for full time Zambian management of KNBC and ZESCO and asked whether it had been decided that the Mines Act should still apply to the construction of Kariba North.

Mr. McNamara questioned the basis for power consumption forecasts, in particular the assumptions as to copper production over the next four or five years. It appeared from the answers given by the Minister and his officials that a very optimistic build-up of copper output to 900,000 tons per annum by 1974 had been assumed and Mr. McNamara asked Mr. Dean to check with MINDECO and get as realistic a projection as possible and relate this to power requirements. Mr. McNamara said that he also wanted Mr. Dean to prepare a timetable of work to be done and who would do it for Kariba North and Kafue II.

Mr. McNamara asked what were the major transport problems which Zambia faced. The Minister said that the country's land-locked position made it necessary for her to develop as many outlets to the sea as possible. Because the main outlets for Zambia were through minority-controlled regimes to the south, Tanzania and Zambia had decided to build the Tazara Railway, which was expected to be completed in 1974 or early 1975. He said that it would be necessary to increase the port facilities at Dar-es-Salaam to cope with Tazara traffic. Mr. McNamara said that the Bank was in the process of making a loan to the East African Railways & Harbours Authority which would be used to construct an additional three berths.

<u>Mr. Arthur Wina, ex Minister of Finance & Education; Mr. Lishomwa, ex Permanent Secretary of Finance & Planning, and Mr. Kasonde, ex Permanent Secretary of Finance</u>

Mr. McNamara asked what in their view were some of the main problems which Zambia faced. They collectively gave a surprisingly accurate account of the financial difficulties facing the country and what needed to be done, by way of pruning capital and recurrent expenditure within a likely level of available resources.

Mr. McNamara asked why there was such a big gap between the commendable intentions and performance in rural development. Mr. Lishomwa said that the main reason was that the political base in the urban area was stronger than in the rural. Messrs. Wina and Kasonde said that it was mainly because development in the rural areas was more difficult to implement than the urban areas. Mr. Lishomwa said that he thought it would be very useful for a respected institution, such as the World Bank, to talk bluntly in private to the government about the need to cut fat programs, to administer them more carefully and to ensure achievement rather than action.

Mr. Mark Chona, Special Assistant to the President

Mr. Chona said that he thought the government over the last few years had made good decisions but was poor in implementation. He thought that there was a number of difficulties causing this and one step towards improving it will be the integration of the Ministry of Finance with Development Planning. He felt the biggest problem was the gap between rural/urban income and that required the government to press ahead with rural development. He said that taxes from the rural sector will for sometime be low and, while the mining company bonds were being repaid, copper revenues will be limited. He said that the farmers in the rural areas can develop without a lot of capital investment; the problem is more to get the people necessary to raise farming standards and to provide infrastructure and social amenities together with rural areas. He thought that the village development programs, the farmers institutes and the functional illiteracy campaign, using night classes, have made great strides in this direction.

RMDean:ls

cc: Messrs. Demeksa/Mekki
Bell
Husain
Kirmani
Clark
Dean
North
van Dijk
Morse
Walton
Ljungh
Dixon
Simmons (Tourism)

RMcN Chron

OFFICE MEMORANDUM

TO: For the Record

DATE: April 21, 1975

FROM: S. Shahid Husain SH

SUBJECT: Meeting with President Kaunda of Zambia, April 19, 1975

On April 19, Mr. McNamara, accompanied by Messrs. Knapp and Husain, called on President Kaunda of Zambia at the Blair House. The Zambia Minister of Finance, Mr. Chikwanda, the Special Adviser to the President, Mr. Lishomwa, and the member of the Central Committee in Charge of Economic Planning, were also present.

President Kaunda recounted the political developments in Southern Africa. He said that with South Africa's intention to withdraw armed personnel from Rhodesia and the projected independence of Mozambique, chances for a peaceful transition to majority rule in Rhodesia had improved significantly. He, however, felt that Governments, particularly big powers like the United States, had to exert sustained pressure to this effect, as well as to the independence of Namibia. The President said that he was a strong believer in peaceful solutions to international problems and the improvement in chances for a peaceful settlement in Southern Africa was largely the result of international opinion. Yet this peaceful transition could not be taken for granted and the effort had to continue until majority rule was secured in Rhodesia and Namibia. Mr. McNamara complimented the President on his statesmanship and diplomacy and said that public organizations and churches in the United States were increasingly conscious of the human and political issues in that region.

4/21

Mr. McNamara then raised the issue of development strategy and policies in Zambia. He said that while Zambia had been beset with many problems, including the initial lack of trained manpower, the neglect of the rural sector would seriously aggravate the economic situation. He expressed his concern at the fact that the whole economy was living off copper, with little effort to improve the employment opportunities and production in the rural sector, where the mass of the people still lived. The severe dualism which this gave rise to could have the seeds of future political and economic trouble. He was particularly concerned with growing food imports, while other claims on copper earnings were increasing. Mr. McNamara said that he had the impression that the President's own commitment to rural development in Zambia was not shared by others in the Government. Policies such as investment allocations, prices of agricultural products and allocation of administrative and managerial resources were still not geared to the welfare of the mass of the Zambian people. There was a heavy bias towards the urban population. Mr. McNamara expressed distress at the fact that two projects, namely, the Mixed Farming Project and the Integrated Development Zone Project, on which substantial manpower had been spent by the Bank, were withdrawn by the Government. The President seemed to be unaware of these decisions. The Finance Minister said that the Government was increasingly shifting resources towards the rural sector; in its price policy it had the problem that any increase in agricultural prices would lead to pressures from the urban population. The strategy, therefore, was to subsidise inputs such as fertilisers and initially to secure output increases from large farmers (mainly expatriates). He also expressed concern that the transport and marketing bottlenecks did not permit rapid increase in agricultural production. The Minister said that the withdrawal of the agriculture projects was largely on account of his concern at the poor implementation of agricultural projects in general in Zambia.

The President invited Mr. McNamara to come back to Zambia to see for himself the changes in the country.

Note: Subsequently, I had discussions with Mr. Lishomwa, Special Adviser to the President, who said that the frankness of Mr. McNamara's remarks was fully appreciated by the President, who shared his concern. I have arranged with Mr. Lishomwa that when our Agriculture Sector Report is ready for discussion with the Government, I would try to go myself to have a full discussion on the rural development strategy with the Government.

cc: Messrs. McNamara, Knapp, Wiehen, Adler

SSHusain:pe

INTERNATIONAL DEVELOPMENT ASSOCIATION | INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: April 17, 1975

FROM: S. Shahid Husain hr

SUBJECT: ZAMBIA: Brief for Meeting with President Kenneth D. Kaunda

1. The President of Zambia, Mr. Kenneth D. Kaunda, is scheduled to meet with you on April 19, 1975. Included in his delegation are three Ministers (Planning and Finance, Foreign Affairs and Education) and a large group of advisers (refer Annex "A"). Two members of the delegation are of special interest to the Bank: Mr. A. B. Chikwanda (Minister of Planning and Finance) is a 34 year old politician from the Copperbelt who has been a Minister for about three years and took his present post in December 1973. Mr. L. M. Lishomwa (Special Assistant to President Kaunda on Economic Affairs) is an ex-Permanent Secretary of Planning; you met him during your November 1972 visit to Zambia; he was active in our discussions with the Government on economic policies, which preceded our program loan, in early 1973.

I. Introduction

2. Since independence in 1964 Zambia has confronted a series of crises resulting mainly from the economy's vulnerability to fluctuations in copper export earnings, the hostile relations with Rhodesia, and disharmony in domestic politics. Despite these problems and the lack of trained manpower, the Government has been fairly successful in developing its power resources, transportation and urban infrastructure and in expanding manufacturing as well as health and education services. However, performance in the agricultural sector has been disappointing, with the result of widening income disparities.

4/17

II. Domestic Political and Administrative Developments

3. In 1973 President Kaunda took two major steps: He launched an effort at reconciliation with his two major rivals (Harry Nkumbula and Simon Kapwepwe) towards building up national unity. And in August of that year, Zambia was constituted as a one-party (UNIP) state. In December 1973 the first general elections were held under this system. President Kaunda, the only candidate, was elected for a third five-year term.

4. The administrative machinery has been overstrained by the large role assumed by the Government in the economy, the rapid advancement of Zambians, and the frequent shuffling of ministers and top civil servants. A newly established Central Committee of the party composed primarily of senior politicians is shaping up as a super-cabinet and unfortunately is further confusing the decision-making process.

III. International Relations

5. President Kaunda and Zambia have enjoyed their greatest success in the field of international diplomacy and politics. President Kaunda and his vigorous Foreign Minister Vernon Mwaanga have played an important role in the political transformation under way in southern Africa. President Kaunda has had a moderating influence on the dramatic chain of events that started early 1974. He has courageously attempted to bring about peaceful change by starting a dialogue between "black" and "white" Africa. His major "accomplishments" have been associated with (a) Mozambique's sprint towards independence (June 1975), (b) bringing the three rival black Rhodesian (Zimbabwe) leaders together while setting in motion the cease fire and negotiations between Rhodesian Prime Minister Ian Smith and the African National Council, and (c) the prospect of a change in South Africa's policy towards Namibia. Zambia's foreign policy setbacks have been: (a) the failure of Minister Mwaanga's candidature for the OAU Secretary General's post after the division of the OAU members along Arab/Muslim and non-Arab/non-Muslim lines; (b) the failure of efforts to unite the three liberation movements in Angola, and (c) the attack by radical African countries on Zambia (along with Tanzania, Botswana, Liberia and "FRELIMO") at the two last OAU Conferences (February and April 1975) for a "too hasty" acceptance of South African Prime Minister John Vorster's overtures regarding "detente". However, most black leaders appear to support President Kaunda's negotiations with South Africa as far as they are aimed at the peaceful transition of Rhodesia to majority rule.

6. In addition to concern for peace and reconciliation in Africa, President Kaunda's efforts may have also proceeded from (a) his desire to secure alternate/cheaper access to seaports in Mozambique and Angola for Zambia's trade; (b) his desire to outflank and contain Zairian President Mobutu's ambitions regarding Angola, and (c) the need to distract his countrymen from growing domestic problems.

IV. Economic Background

export

7. The Zambian economy continues to be dominated by copper, which accounts for about 40% of real GDP and over 90% of copper earnings. The economy is characterized by extreme dualism between a large modern sector and a rural subsistence sector, with incomes per head in the former about five to six times those in the latter. The result has been rapid urbanization during the decade (from 10% to 32% of the total population) and in the last two years increasing evidence of unemployment. During 1964-74 real GDP grew at a 4% average annual rate (1964-69: 5.7% and 1969-74: 2.2%). With the population growing at 2.9% per annum, real GDP per capita has fallen since 1969. Real gross national income per head is presently about $350. The performance of the important sectors of the Zambian economy has been mixed:

	Share of Sector in 1974 GDP	Growth Rates 1964-69	1969-74
Agriculture	10.5%	1.0%	2.0%
Mining	40.9%	3.0%	-0.5%
Manufacturing	13.2%	15.0%	11.5%

8. The balance of payments showed a modest surplus in 1974 ($45 million) despite a large increase in imports both in volume and in prices. Oil imports increased (almost threefold over the 1973 level) to $71 million. Due to a fall in copper prices since April 1974 (from a historic high of $1.37 per pound to $0.59), foreign reserves fell from a June 1975 peak of $360 million to about $150 million (hardly two months' imports) by February 1975. Given the Bank's projections for slow economic recovery in OECD countries and a lagging demand for copper, Zambia will not be able to sustain the same pattern of economic policies. This will require a recognition by the Government that it has to recast major parts of its economic strategy.

9. The 1975 Budget projects a small deficit on recurrent account. With the proposed increase in capital expenditures there would be a large over-all financial gap (about 30% of total Government expenditures), only half of which would be covered by prospective external and domestic non-inflationary borrowing.

10. Past and prospective Bank Group activities are described in Annexes "B" and "C", respectively.

V. Major Problems Facing the Zambian Economy

11. Two major problems face Zambia and unless seriously grappled with will soon reach critical proportions: (a) lack of rural development and slow increase in agricultural production, and (b) misallocation of resources.

Agricultural and Rural Development

12. There is dualism in the rural sector between large and medium scale commercial farmers, many of whom are expatriates, and small traditional farmers. The Government has not yet devised a strategy to cope with the problem of dualism which it perceives as reflecting conflicting interests. The appropriate strategy should be directed both towards improving the situation of the rural poor and increasing agricultural production. First, the neglect of the rural areas cannot be continued any longer because:

(a) 68% of the population still lives there;

(b) the rural-urban income disparity is sucking the young into the town (urban growth is still as high as 7% per annum) while employment lags behind; and

(c) the rural population is becoming acutely aware of the imbalance.

Despite high level pronouncements about the Government's commitments to rural development, the big thrust in directing resources (administrative and financial) to the rural areas has not taken place.

13. Second, a well-planned development of agriculture is needed to:

(a) stem the rapidly rising food import bill (now $~~90~~ 60-70 million per annum);

(b) create new employment; and

(c) diversify the economy while decreasing the present dependence on mining.

Fortunately, large increases in agricultural production do not present insuperable problems in Zambia as sufficient good land is available. However, success in agriculture would require a shift in investment priorities, changes in the pricing of agricultural products, more effective provision of inputs, and better marketing of products. The Government has recently increased the price of some agricultural commodities but much more needs to be done.

14. The Government has repeatedly claimed that it lacks implementing capability. To suport this contention Government representatives cite the failure of the Bank-financed livestock project ($2.5 million loan of FY69 which was cancelled and fully prepaid in FY74), two projects financed by the African Development Bank, and a Yugoslav-financed project. The Bank has attempted to assist the Government by a large input of staff time in preparing projects. Two agricultural projects were fully prepared and appraised by us but Government recently withdrew both. These projects envisaged setting up implementation units with some expatriate staffing. The difficulties, however, are not merely related to the shortage of trained manpower but also to improper utilization of staff and lack of leadership. The Ministry of Rural Development provides insufficient guidance, its planning is inadequate and its coordination with other Government departments is poor. The Government simply is not giving this sector the priority it deserves. We recently organized a rural development and agricultural survey designed to help the Government identify policy options and devise appropriate strategies and institutions.

15. Resources - Better management of resources is also desperately needed:

(a) Despite a high level of investment (averaging some 25% of GDP over the last decade) domestic production increased by less than 3% a year during the last five years while unemployment expanded; clearly a more rigorous assessment of proposed investments is desirable.

(b) The rapid increase in recurrent expenditures has led to a situation where Government savings are negative or low (except in years of high copper prices) necessitating curtailment of Government development programs. This increase was due initially to rapid raises in Government wages and salaries and defense expenditures and more recently to large subsidies (budgeted at more than $100 million in 1975) a large part of which were in support of urban consumer goods.

(c) The failure to build up foreign exchange reserves in good times to safeguard economic development at times of low copper prices.

VI. Issues You May Wish to Raise

16. We have repeatedly drawn the attention of Government to the need (a) for according a higher priority to rural development and for strengthening the administrative and executive capacity in this sector and (b) for a better husbanding and use of its resources. In our past discussions on economic policy we have not attempted to establish specific performance criteria. We propose to intensify our general dialogue during the forthcoming basic economic mission (June 1975) and the discussions of the draft "Rural Development Sector Survey" which are scheduled for July 1975. It is clear, however, that if Bank lending is to continue at the proposed levels, the Government must take concrete steps to tackle the two major problems outlined in paras 11-15 above.

VII. Point that President Kaunda's Delegation May Raise

17. President Kaunda may request that the Bank consider another program loan in view of the depressed copper prices and the increasing cost of fuel and food imports. We feel that Zambia should use the IMF facilities for its short-term needs, while we continue to assist by considering any feasible project proposal.

Attachments

cc: Mr. Knapp

SAWMoini/MHWiehen:cj

ANNEX "A"

ZAMBIAN PRESIDENTIAL DELEGATION TO WASHINGTON

1. His Excellency the President, Dr. Kenneth David Kaunda
2. Hon. Vernon J. Mwaanga, Minister for Foreign Affairs
3. Hon. Fwanyanga M. Mulikita, Minister of Education
4. Hon. Alexander B. Chikwanda, Minister of Planning and Finance
5. Mr. Lishomwa M. Lishomwa, Special Assistant to the President (Economics)
6. Mr. Patrick J. Chisanga, Secretary to the Cabinet
7. Dr. Henry S. Meebelo, Director of Research, Party Headquarters
8. Mr. Julian L. Msaninga, Permanent Secretary, Ministry of Foreign Affairs
9. Mr. L. E. Kawesha, Under Secretary, Ministry of Planning and Finance
10. Mr. A. T. Mpengula, Director for American Affairs, Ministry of Foreign Affairs

RECENT BANK GROUP ACTIVITIES IN ZAMBIA

Lending. The Bank has made 17 loans amounting to about $400 million (net of cancellations) and IFC 2 investments amounting to $2.3 million in Zambia. Bank lending to Zambia during the last three years (through FY75) of $284 million makes it the third highest borrower per capita ($21) from the World Bank Group for the FY73-75 period.

		Total Amt.in FY
FY 1973:	Third Education project: $33.0 million Integrated Family Farming project: $11.5 million Program Loan: $30.0 million	$74.5 mil.
FY 1974:	Kafue Hydroelectric Power project: $115.0 mil.	115.0 mil.
FY 1975:	Lusaka Site & Services & Squatter Upgrading project: $20.0 million Kariba North Power Generation (Supplementary) loan: $42.1 million Telecommunications project: $32.0 million Scheduled for Board presentation May 1975 (not included in aggregates above)	94.1 mil.

Other Activities. During FY74-75 we undertook the following surveys/studies: (i) Urban sector survey in September 1973; (ii) Water Supply (domestic, commercial and industrial use) sector survey in September 1973, in cooperation with WHO; (iii) Agricultural & Rural Development sector survey during September-November 1974, in cooperation with FAO.

In January 1974 our one-man resident mission was established in Lusaka.

PROPOSED BANK GROUP ACTIVITIES IN ZAMBIA

Lending Program

As two (already appraised) projects in the agriculture sector (Mixed Farming and Intensive Development Zone) were dropped at Government's request

we may have a much lower level of lending in FY76. During the next three years, however, we propose an average of $65-70 million per annum of lending to Zambia.

FY76 - Second Forestry project (plantation and processing): $15.0 million
Development Bank of Zambia: $15.0 million

FY77 - Kafue III (hydroelectric power development project): $40.0 million (may be advanced to FY76)

- Fourth Education project: $25.0 million
- Second Urban project: $20.0 million
- Third Roads (construction and maintenance): $15 million
- Water Supply project: $15.0 million

FY78 - Agriculture (unidentified) project: $25.0 million
- Second Telecommunications project: $35.0 million
- Second Loan to Development Bank of Zambia: $20.0 million

Other Activities

An economic mission is scheduled for June 1975. At the request of the Government it would cover inter alia the mining and industries sectors as a prelude to possible Bank assistance in these sectors. In July 1975 we propose to discuss the report of the "Agricultural and Rural Development Sector Survey", undertaken in autumn 1974, and thereafter assist the Government in evolving a coherent policy for the sector. In response to Government request a transport sector survey is proposed for autumn 1975.

766.

WORLD BANK / INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: Records

DATE: May 22, 1978

FROM: Michael H. Wiehen, Director EACPI

SUBJECT: Meeting between President Kaunda of Zambia and Mr. McNamara - May 19, 1978

1. On Friday, May 19, 1978 Mr. McNamara met with President Kaunda at Blair House over breakfast. Also present were Messrs. Mwanakatwe, Minister of Finance; Dominique Mulaisho, Economic Adviser to President Kaunda; Lloyd Sichilongo, Under-Secretary in the Ministry of Finance; Wila Mung'omba, Executive Director for Zambia in the IMF; Mr. Wapenhans, and myself.

2. Mr. McNamara opened the formal discussion by reminding President Kaunda of their last meeting, three years ago, at which they had agreed that Zambia needed to do a lot more to strengthen agriculture, and said he was very pleased to learn that since then the Zambian Government had taken or initiated a number of important measures toward that objective. He referred particularly to repeated producer price increases and also commented favorably on the fiscal and monetary changes the Government has implemented. He stressed once again the importance of agriculture in the Zambian Government's plan to diversify the economy. He underlined the fact that, in view of the slow growth in the industrial countries, the copper price was likely to remain depressed for some time to come and that, therefore, Zambia would have to pursue all other possibilities, internal and external, for mobilizing resources for development. He expressed his hope that the forthcoming Consultative Group meeting would help Zambia in this effort to raise quick disbursing aid and that Zambia would proceed quickly with finalizing the Third National Development Plan, so that a second meeting of the Consultative Group could be convened early in 1979 to discuss international support for Zambia's longer term investment program.

3. President Kaunda confirmed the strong emphasis given by him and his Government to agriculture. He acknowledged and thanked Mr. McNamara for all the assistance that the Bank is giving Zambia at the present time, particularly in the formation of the Consultative Group. Regarding the Third National Development Plan, President Kaunda said that for obvious reasons work on the Plan had been suspended last year, but preparations were now again in full swing and the Plan should be ready later this year. He said that Zambia needed very substantial help in translating the Plan proposals into action and he asked the Bank for its technical assistance in this endeavor. Mr. McNamara responded by saying that the Bank realized the great need for technical help and was prepared to assist Zambia in mobilizing such help. He said the Bank Group could finance experts for project preparation as well as project

implementation and perhaps also on the planning side. President Kaunda assured Mr. McNamara that his Government did not harbor any reservations regarding expatriate technical assistance and will have to accept the need for higher remuneration of such experts.

4. I reported briefly on the meeting I had had the day before with Mr. Chikwanda, Zambia's Minister of Lands and Agriculture, and on our agreement that Mr. Chikwanda would prepare a comprehensive program of technical assistance required by his Ministry; the Government and we together would thereafter collaborate in mobilizing external resources to provide this technical assistance, including a possible technical assistance credit by the Bank Group. I added that the Government had been in discussions with Canada for some time on the provision of a few technical experts for the Agriculture Ministry, but that these discussions had not yet led to any concrete results. Mr. McNamara offered to contact the Canadian Government, if this were necessary, in order to speed up the availability of such technical assistance.

5. Mr. McNamara said that in view of Zambia's immense need for technical expertise from abroad, it was important that the remuneration offered to expatriates was sufficient to attract the necessary number and quality of experts. President Kaunda acknowledged this; he added that in view of Zambia's fiscal problems it had been necessary to increase the tax burden on expatriates resident in Zambia.

6. Mr. Wapenhans commented on the export-import transport crisis which has rather rapidly become another serious problem for Zambia, and said that according to recent reports it takes 16 to 18 months for some goods to be delivered from Dar es Salaam to Lusaka. President Kaunda confirmed that because of the closure of Zambia's traditional export links through Angola and Rhodesia/Mozambique, and because of substantial logistics problems on the major new transport route through Dar es Salaam, a critical situation had indeed developed. He said that major efforts were underway to speed up transport through Tanzania. Mr. Wapenhans explained that the Bank was closely collaborating with the UN in their efforts to assess the transport problems and design measures for dealing with them. President Kaunda added that Zambia was considering to ask Canada for help to extend the Nacala-Lilongwe-Mchinji railway to Chipata, the commercial center in eastern Zambia, in order to provide an additional link with the sea.

7. The conversation ranged over a number of other subjects not directly related to Bank operations.

8. In closing, Mr. McNamara assured President Kaunda of the Bank Group's full support in Zambia's development efforts. President Kaunda once again thanked Mr. McNamara for the consistent help the Bank has given to Zambia.

cc: Mr. McNamara (2)
Mr. Knapp
Mr. Wapenhans
Mr. H. Adler
Mr. Gulhati
Mr. O'Brien
Mr. Reese
Mr. Jalil
Mr. Thahane

MHWiehen/WAWapenhans/msg

WORLD BANK / INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara DATE: May 18, 1978

FROM: Willi A. Wapenhans *wq.*

SUBJECT: ZAMBIA - Visit of President Kenneth Kaunda

1. President Kaunda is visiting the USA on a state visit. Accompanying him are five Ministers (Foreign Affairs, Finance, Lands and Agriculture, Mines, and Economic and Technical Cooperation) and a large group of advisers (Annex 1), two of whom are of special interest to the Bank:

> John Mwanakatwe, Minister of Finance, a powerful government civil servant for many years and the man President Kaunda turned to in 1976 to handle Zambia's worsening financial crisis, he has worked closely with the Bank and will head the Zambian delegation to the Consultative Group;
>
> Alexander Chikwanda, former Minister of Finance and now at Lands and Agriculture, he has spearheaded the Government's new emphasis on agricultural production and has provided support for our project preparation activities.

We plan a separate working session with the Minister of Finance in preparation of the Consultative Group meeting scheduled for June 27-29.

Purpose of Visit

2. As you know, Zambia is in the throes of a prolonged economic and financial crisis brought on by its continuing dependence on copper and the depressed state of copper prices from 1975 to the present. We understand that the purpose of President Kaunda's visit to England and the United States is to present his country's case for substantial increases in concessionary resources from Zambia's traditional supporters (Press reports of President Kaunda's and Prime Minister Callaghan's meeting in London on May 15 state Britain will pledge about $30 million in additional aid at the Consultative Group meeting next month).

Magnitude of the Current Economic Crisis

3. Copper production continues to contribute over 20 percent of real GDP, more than 90 percent of export earnings, and (in years of good copper prices) as much as 40-50 percent of government revenues. The impact of three years of depressed copper prices on the budget, balance of payments, and production can be summarized as follows (Annex 2 provides a fuller description of the economy and the current situation):

(a) the decline in mineral tax revenues from K 339 million in 1974 to zero in 1977 and 1978 has led, despite government efforts to cut expenditures and raise non-mineral tax revenues, to large budgetary deficits, which have been heavily financed through the monetary system and contributed to inflationary pressures (price increases have accelerated from 10 percent p.a. in 1975 to about 20 percent p.a. in 1977);

(b) despite tight import controls, current account deficits totalling K 652 million have been accumulated during 1975-77; because net capital flows were insufficient, these deficits were financed mainly through an accumulation in arrears in payments for imports and private remittances (amounting to SDR 393 million at the end of 1977 and SDR 467 million at the end of March 1978) and a reduction in net foreign assets from K 77 million to minus K 173 million; and

(c) shortages of essential imports of raw materials and spare parts (imports of which fell 32 percent between 1975 and 1977) have created idle capacity in many sectors and contributed to a decline in real output; while GDP fell by two percent between 1975 and 1977, declines were larger in the sectors most severely hit by import restrictions - manufacturing (11 percent); construction (14 percent); transport, communications and storage (26 percent) and wholesale and retail trade (12 percent).

4. Due to poor copper price prospects plus the need to pay off arrears and build up foreign exchange holdings, the next 2-3 years will be difficult ones for Zambia. A minimum capital inflow of $1.2 billion is needed in 1978-80 to cover projected current account deficits, pay off arrears and build up net foreign assets to zero. This provides for no real growth in imports, thus perpetuating existing shortages; to permit an adequate growth of imports of essential raw materials and spare parts sufficient to restore and maintain full utilization of capacity, a $2 billion capital inflow would be required.

Government's Response

5. As the bleak prospects for improved copper prices in the short and medium term became apparent, the Government adopted a series of tough policies, many at the expense of the powerful urban constituency, to curb expenditures and promote agricultural and industrial production. Some of the important steps taken are (Annex 3 provides a comprehensive description of these measures):

(a) measures to reduce the budgetary deficit: by holding the growth of recurrent expenditures to two percent p.a. (mainly through large reductions in subsidies), cutting capital expenditures by 30 percent, and increasing taxes on income and customs/excise/sales taxes by 71 and 85 percent respectively, the Government has been able to reduce its deficit by 50 percent and the annual amount borrowed from the banking system by 67 percent between 1975 and 1978;

(b) measures to diversify the economy: the Government has sharply raised agricultural producer prices and significantly increased its budgetary investment in the rural sector (thus increasing the share of agriculture in its capital budget from 13 to 18 percent). It has also passed an Industrial Development Act which provides tax incentives for investments designed to promote the Government's objectives for industry (e.g., industrial exports, employment creation, utilization of local resources, location in rural areas). Two devaluations totalling 23 percent (in 1976 and 1978) will reduce the bias against exports and, together with tight wage restraints, promote more labor intensive techniques.

International Response

6. The international community has responded to Zambia's needs, particularly as the economic situation has worsened. In July 1976, the IMF approved a standby arrangement equal to $71 million and in September of the same year the Bank approved a $30 million program loan (Ln. 1322-ZA). However, Zambia was unable to meet the IMF performance criteria and did not draw on the standby funds. Despite this difficulty, Zambia maintained good relations with the IMF and earlier this year negotiated a major standby agreement, which, owing to the country's "exceptional circumstances", involved waiving the limitations that the country's quota would normally impose upon drawings. The standby, together with resources from IMF's Compensatory Financing Facility and Trust Fund, would provide over $380 million in external resources during 1978-80. Bank and Fund staff have cooperated closely during the period of Zambia's difficulties; the Fund negotiated the standby with the assumption that the Bank would give sympathetic consideration to a request for program assistance. Nonetheless, substantial additional resources on appropriate terms from other multilateral and bilateral sources will be needed to pay off arrears and build up foreign exchange holdings, as well as allow an expansion of essential imports and hence a resumption of economic growth. To help with this task, the Government has asked the Bank to form a Consultative Group for Zambia. The Consultative Group's first meeting, scheduled for June 27-29, 1978, is expected to focus on the country's financial crisis and the Government's medium-term policies and programs for guiding the economy back to normalcy. A second meeting in early 1979 is expected to follow the publication of the Third National Development Plan.

ISSUES

7. Plan. Completion of the Third National Development Plan (TNDP), scheduled to run from 1978 to 1982, was postponed last year while the Government focused its energies on coping with the rapidly deteriorating economic conditions. Considering the circumstances, we believe the Government made the correct decision; however, to provide a medium term prospective for the Consultative Group, the Government has prepared an approach paper for the TNDP, including the Plan's objectives and an outline of the investment strategy. It is important that the Government

complete work on the TNDP as quickly as possible to form a basis for (a) a possible Bank program loan, (b) a second Consultative Group Meeting in early 1979 to focus on long-term development prospects, and (c) mobilization of project-oriented resources. In your discussion with President Kaunda you may wish to indicate the importance we attach to the completion of the TNDP.

8. Strengthening the Performance in the Agricultural Sector. As you know, the absence of determined efforts to diversify the economy by placing emphasis on agricultural production and rural development has long been of concern to the Bank. The Government now has taken first steps to strengthen agricultural production; it has substantially increased producer prices, established a project preparation unit in the Ministry of Lands and Agriculture, begun preparation of projects in cash crops such as coffee, cotton, tea and oilseeds, and arranged with the Canadian Government to obtain technical expertise for project planning and analysis. Despite these measures, the Government's agricultural institutions require substantial strengthening:

- the Ministry of Lands and Agriculture has numerous vacancies at technician and administrative levels, many requiring skilled expatriates;

- there is an immediate need for a sectoral plan to provide a basis for allocating the Government's limited resources;

- the Government should take steps to strengthen the agricultural capabilities of the provincial ministries, and the relevant parastatals; and

- the Government should accept offers of technical assistance funds to improve its ability to identify and prepare agricultural projects.

We have advised the Government that we would be prepared to consider a $4-5 million technical assistance credit to finance preinvestment work especially in agriculture and rural development and to establish a project preparation unit which would work with the operating ministries (mainly Agriculture and Industry). This is designed to increase the absorptive capacity of Zambia for capital assistance since other main donors appear to be similarly inclined towards financing primarily high priority agricultural projects.

9. Industry. The Government needs to focus its industrial policies to encourage production based on domestic resources instead of the current emphasis on consumer goods which require high levels of imported raw materials and intermediate goods. The Government has taken some initial steps (e.g., a new Industrial Development Act) to stimulate industrial growth, particularly in the private sector, which for years has stagnated

due to increasing state control over industrial production. Although recent Government pronouncements have encouraged foreign and local private investment, the Government has not made the necessary changes in tariffs and prices, nor provided other incentives to stimulate industrial growth. The Government should be encouraged to continue its efforts to expand the industrial base and to implement the required industrial policies. To help Zambia with its industrial efforts, the Bank has: (i) sent a recent mission to examine agro-industry possibilities; (ii) arranged for a UNIDO mission late this year to investigate industrial opportunities using local resources; (iii) scheduled an updating economic mission for later this year to review the Government's policies and incentives to promote industrial development.

10. Expatriate Remuneration. To accomplish its program for restructuring the economy and to enhance its absorptive capacity, Zambia will require substantial technical assistance, particularly planners and technicians in agriculture and industry. The Government accepts this fact in principle, but, with the exception of the state-controlled copper industry where competitive international salaries are paid, the Government has been very reluctant to budge from its existing policy limiting expatriate salaries to the same levels as those in the civil service. This has made it increasingly difficult to recruit qualified expatriate staff, particularly for agriculture and industry, other than under bilateral grant assistance programs. We have raised this issue with senior Government officials over the last two years pointing out the inconsistency of this policy with its objectives of expanding agricultural and industrial production, but have not obtained broad agreement on the Government's willingness to accept international levels of compensation for expatriates. The Government needs to weigh the advantages of obtaining technical assistance it requires in the agricultural and industrial sectors and thereby enhancing its prospects for diversification and growth against the mainly political disadvantages of being seen to pay competitive remuneration for expatriate services. While Zambia should avail itself of grant-financed technical assistance to the extent possible, a more flexible approach to expatriate compensation is nevertheless essential. The discussions on and the delays in the recent Zambia Highway Maintenance project, as well as difficulties we have experienced recruiting expatriates for our ongoing power and family farming projects, are typical examples of the problems encountered in this area.

11. Bank Group Operations. The Bank recently provided Zambia with its first IDA credit (Third Highway Project, approved by the Board on May 11, 1978, $11.25 million IDA/$11.25 million Bank). The FY79-83 program contains 14 projects for $259 million ($205 million Bank, $54 million IDA) of which seven are in agriculture (totalling $100 million). The IFC has recently appraised a complex $250 million copper project, and in his memorandum to you of March 30, 1978, Mr. Qureshi sought (and subsequently received) your approval to continue processing the project. Details of the Bank's proposed program and the issues concerning the IFC project are contained in Annex 4.

12. Program Loan. Given that the purpose of President Kaunda's visit is to mobilize short-term financial support, we would expect him to ask about the prospects for a new program loan. Earlier this year Mr. Mulaisho, Special Assistant (Economics) to President Kaunda, wrote and asked on what conditions the Bank would consider providing a new program loan for Zambia. We responded that if the following steps were taken, the Bank would be willing to consider a small program loan:

a) 1 Zambia reached agreement with the IMF for a standby program, and remained eligible for drawings under such a standby,

b) 2 an appropriate multi-year development plan were prepared,

c) 3 steps were taken to strengthen agricultural production (maintaining an appropriate price structure, initiating intensive efforts to prepare and implement projects, and strengthening the Ministry of Lands and Agriculture, agricultural planning at the provincial level, and the agricultural parastatals),

d) 4 a development equalization account was established in the Bank of Zambia and the ground rules for operating the account were agreed upon, and

e) 5 industrial policies were thoroughly examined (including prices, tariffs, taxes, institutional structures, etc.) and revised to encourage industries based on agricultural inputs and other local resources.

The Government has already met some of these conditions, including agreement on an IMF standby. It is essential that the Government continues to meet the standby's performance criteria, not only to meet a condition for our program lending, but because a working IMF agreement will be the core of any package of international assistance to meet Zambia's immediate financial needs. The two program loan conditions which should be emphasized at this time concern preparation of 1 the development plan and further 2 strengthening of agricultural institutions. We have tentatively allocated $25 million for a Third Program Loan in Zambia's FY79 lending program 1/ and propose to supplement that with the $3 million allocated to Zambia under the EEC Special Action Fund. We would not expect to appraise the loan until after the Consultative Group has met, and progress made on preparation of the Plan. The proposed Program Loan, while small in relationship

---

1/ Post script to the country issues paper discussed with Mr. Knapp on March 30, 1978 is attached as Annex 5.

to Zambia's 1978-80 needs ($1.2-$2.0 billion), must be examined in light of the Government's expectations. The Government has arranged a $380 million IMF standby and hopes to mobilize $400 million through the Consultative Group (the British will pledge $30 million, the Bank has the program loan to offer; overall, we think the prospects for reaching Government's target appear fairly good). This leaves $400 million - $1.2 billion for the Government to raise in the next 18-24 months. Clearly the Government will be hard pressed to raise the additional concessionary assistance, but we feel it may be possible if the Government can implement its new economic policies.

Attachments

RSullivan/WMcCleary/si

Annex 1

Delegation

1. President Kenneth David Kaunda
2. Hon. Siteke Mwale, Minister of Foreign Affairs
3. Hon. John Mwanakatwe, Minister of Finance
4. Hon. Alexander B. Chikwanda, Minister of Lands and Agriculture
5. Gen. Kingsley G. Chinkuli, Minister of Mines
6. Hon. Lily Monze, Minister of State, Economic and Technical Cooperation
7. Mr. Dominic Mulaisho, Special Assistant to the President (Economics)
8. Mr. J. Punabantu, Special Assistant to the President (Press)
9. Mr. Mark Chona, Special Assistant to the President (Political)
10. Mr. C.M. Sikazwe, Principal Private Secretary to the President
11. Mr. E.I. Willima, Deputy Secretary to the Cabinet
12. Mr. M. Liswaniso, Chief of Protocol
13. Mr. H. Nzunga, Permanent Secretary, Ministry of Foreign Affairs
14. Mr. I. Sikazwe, Permanent Secretary, Ministry of Health
15. Mr. Lloyd Sichilongo, Undersecretary, Ministry of Finance
16. Mr. J.C. Mandona, Undersecretary, Ministry of Economic & Technical Cooperation
17. Hon. Rouben Kamanga, Member of the Central Committee
18. Mr. H. Ngwane, General Manager, Rural Development Corporation
19. Mr. G. Mbulo, Director of Research, Bank of Zambia
20. His Excellency Putteho Ngonda, Ambassador to the U.S.

Characteristics of the Zambian Economy and the Effects of the Current Financial Crisis

1. The Zambian economy represents a classic case of economic dualism with a technologically sophisticated, largely urbanized modern sector existing side by side with a traditional and relatively poor subsistence sector. The modern sector is centered around the copper mining industry, a small but rapidly expanding manufacturing sector, a commercial farming sector (heavily dominated by expatriates) and a relatively large services sector. The rural sector comprises 62 percent of the population and is characterized by low productivity and standards of living. Since independence, growth and development has been concentrated in the monetized, mainly urban sector, while the rural sector has stagnated. The Government has not devoted sufficient resources to rural development and, in addition, a Government policy of suppressing agricultural producer prices to keep food prices low (substantially reversed in recent years), in combination with tariffs and quotas on manufactured imports, turned the domestic terms of trade against agriculture and provided a powerful incentive for the production of urban over agricultural goods; as a result, agricultural production did not keep up with domestic demand and Zambia imported many agricultural goods that could have been produced at home (e.g., wheat, rice, dairy products). The substantial disparity in rural-urban incomes has led to rapid migration, worsening the unemployment problem in the major urban centers. The unemployment problem has been excacerbated by rapid population growth, a growing capital intensity in production techniques and, in recent years, declining growth in the modern sector.

2. Despite a declining trend in copper's contribution to GDP due mainly to technological factors (e.g., declining ore grades, greater depth in mining activities), the dependence of the economy upon mining remains high: copper mining contributes slightly over 20 percent of GDP (in contrast to 41 percent in 1965), over 90 percent of export earnings, and -- in good years -- 40 to 50 percent of Government revenues. The continuing heavy dependence upon copper mining has rendered the economy highly vulnerable to fluctuations in international copper prices and perpetuated the illusion that Zambia was a wealthy economy. The well-known volatility of copper prices has made budgetary and foreign exchange resources highly variable and unpredictable; several recent studies have shown that Zambia's exports earnings are among the most unstable of any country in the world. However, so long as copper prices fluctuated about an upward trend (as was true during the first six years following independence), the illusion of wealth freed Zambia from many constraints faced by LDC's: e.g., (i) diversification did not have to be pursued vigorously because foreign exchange was available to pay for imports of food, raw materials and intermediate goods, etc.; (ii) consumption by the Government and the urban classes could be allowed to expand rapidly; and (iii) the Government did not have to pay much attention to parastatal efficiency since operating losses could be covered by budgetary subsidies and loans. The period since 1970 has exposed the fallacy in this view: in

no year since 1970 has Zambia's terms of trade been as high as during 1966-70 period and the foreign exchange and budgetary resources have dwindled. The copper price slump that began in 1974 has made the lesson even more clear.

3. The protracted slump in copper prices has had a profound effect upon the Government's budget, balance of payments and economic activity. Mineral tax revenues fell precipitously from K 339 million ($525 million) in 1974 to K 59 million in 1975, K 12 million in 1976 and zero in 1977 and 1978. Despite successful Government efforts to hold the line on recurrent expenditures, cuts in capital expenditures and increases in non-mineral tax revenues, the Government has been unable to offset the decline in mineral revenues and the resulting budgetary deficits have been mainly financed through the banking system. Such financing, in combination with falling domestic production and a lower volume of imports, has contributed to inflationary pressures; the pace of inflation has accelerated from 10 percent in 1975 to 19 percent and 20 percent p.a. in 1976 and 1977.

4. The decline in foreign exchange earnings from copper has led to massive balance of payments deficits since 1975. Despite tight import restrictions during 1975-77 (which, when combined with a rapid increase in import prices averaging over 20 percent p.a., resulting in a sharp decline in real imports), current account deficits of K 393 million, K 41 million and K 218 million were registered in the three years, respectively. Because net capital inflows fell far short of the amounts necessary to finance such deficits, the deficits were financed by an accumulation of arrears in payments for imports and private foreign remittances and a reduction in foreign exchange holdings. From zero at the end of 1974, arrears accumulated to SDR 393 million at the end of 1977 and SDR 467 million as of March 31, 1978. Between the year-ends of 1974 and 1977, net foreign assets of the monetary authorities and commercial banks fell from K 77 million to minus K 173 million and gross official holdings of international reserves from K 132 million to K 56 million. Because official reserve holdings have now been reduced to below the minimum necessary operational levels (the end of 1977 figure being the equivalent of less than a month's worth of imports), it is no longer possible to finance balance of payments deficits through a decumulation of reserves and, in fact, a reserve build-up would be highly desirable.

5. The foreign exchange shortage has led to a drastic reduction in essential imports. The Government, through its import licensing system, has attempted to shift the composition of imports away from consumption goods toward intermediate and capital goods; thus, between 1975 and 1977, the volume of consumption imports fell by 65 percent while the volumes of capital goods and intermediate goods fell by 42 and 32 percent, respectively. The resulting shortages of essential raw materials, spare parts and other intermediate goods has created idle capacity in many sectors and contributed to the decline in aggregate real output; while real GDP declined by 2 percent between 1975 and 1977, the largest sectoral declines were in manufacturing (11 percent), construction (13.8 percent), transport, communications and storage (25.8 percent) and wholesale and retail trade (11.6 percent), all sectors severely affected by import restrictions.

Government Response to Zambia's Economic Crisis

With the onset of the current crisis, the Government has taken a number of measures to reduce the level of aggregate demand and curb inflationary pressures and intensified its efforts to encourage the diversification of the economy and the fuller and more efficient use of domestic resources:

Budgetary and Credit Measures

- Between 1975 and 1978, the growth of recurrent expenditures has been reduced to 2 percent p.a. (in contrast to the 15 percent p.a. average rate for 1965-75), considerably less than the rate of inflation. Subsidies have been reduced by almost 50 percent (mainly through large increases in the prices of fertilizer and basic foods such as maize meal, wheat flour and bread), while the volume of productive government services (including such activities as education and health, road maintenance and agricultural extension) have declined.

- Budgetary capital expenditures have been reduced by 30 percent, thus severely restricting the Government's development effort; taking into account inflation, such expenditures in 1978 will be the lowest since independence.

- The Government has continued and intensified its long-term efforts to diversify the tax base by expanding non-mineral revenues through higher personal and company taxes and higher rates and expanded coverage for customs duties, excise and sales taxes; since 1974 income tax revenues have grown by 71 percent while customs, excise and sales tax revenues have increased by 85 percent.

- As a consequence of the foregoing, the size of the budgetary deficit has been reduced by 50 percent and the annual level of Government borrowing from the banking system by 67 percent between 1975 and 1978; these measures are expected to substantially reduce inflationary pressures in 1978.

- With respect to money and credit policies, the measures to reduce the size of Government budgetary deficits and to improve the profitability of the mining companies (see below) will slow the growth of the money supply and ease inflationary pressures. In addition, the Government has announced its intention to restore positive real interest rates in order to encourage private savir and reduce incentives to use capital-intensive production techniques; this policy is to be implemented through a combination of interest rate increases (such as those announced on May 1, 1978) and a reduced rate of inflation. Nonetheless, the Government will maintain preferential rates of interest to stimulate investment in agriculture and manufacturing.

Measures to Diversify the Economy

- Since the 1974/75 growing season, the Government has significantly increased agricultural producer prices for major crops (e.g., maize, cotton, ground nuts), contributing, together with generally favorable weather conditions, to a growth rate of 4.6 percent p.a. in agricultural value added from 1974 to 1977. Both commercial farmers and medium-sized Zambian farmers have been helped by higher prices and have responded by expanding production. The Government is committed to reviewing all agricultural producer prices annually and to maintaining adequate production incentives for farmers.

- Despite budgetary stringency, the Government is devoting increased resources to agriculture: while total Government investment will decline between 1977 and 1978, investment in agriculture will increase by 40 percent, raising its share in the total from 13 to 18 percent.

- The Government has also taken steps to strengthen agricultural institutions. In April 1977, it transformed the Ministry of Rural Development into the Ministry of Lands and Agriculture under a dynamic new Minister; it has also created a project preparation unit within the Ministry. As a consequence, our relationships with the Ministry have been improving. We have just appraised a coffee project and have a cotton project scheduled for FY 79. We also have an agro-industrial identification mission currently in the field to determine the possibilities for such investment and the potential for expanding agricultural production to supply needed inputs. In addition, the EEC (with whom we are co-ordinating) is studying and preparing projects for cotton, tea, rice and oil seeds.

- The Industrial Development Act, passed in August 1977, gives assurances against nationalization for foreign and domestic private investors and provides tax incentives for investments designed to promote the Government's goals for the industrial sector - namely, the export of manufactured goods, utilization of domestic raw materials, increased employment, the development of local industrial skills and location of industry in rural areas.

Measures to Increase Efficiency and Domestic Resource Utilization

- Since July 1976, the Kwacha has been devalued twice by a total of about 23 percent, increasing the competitiveness of Zambian products, thus promoting exports and import substitution while increasing the relative cost of imported capital goods.

- The 1978 devaluation and a number of cost cutting measures will allow the two mining companies to break even in 1978 and begin generating profits in 1979 (even at the relatively low copper prices projected for those two years); among the cost cutting measures are - reductions in operations at costly mine sites, cutbacks in administrative overhead costs, better inventory controls and some labor force reductions.

- The Government is committed to increased efficiency and "economic pricing" by parastatals to allow those enterprises to generate resources for investment and increased tax revenues, while reducing their dependence on the Government's budget for subsidies. A number of recent price increases (e.g., for maize meal, wheat flour, cooking oil) have reduced subsidies and improved the financial position of many parastatals but a continued effort is needed. The Parastatals Bodies Services Commission, appointed by President Kaunda in 1977, has begun monitoring the activities of the parastatals and making appropriate recommendations, but the activities of the Commission have been limited by the lack of skilled personnel.

- Continuing the policy of general wage restraint which has led to a decline in real wages in the modern sector since 1972, the Government has placed a wage freeze on all civil service salaries in 1978 while limiting parastatal and private sector increases to those allowable under existing contracts (generally under 5 percent, substantially less than the expected inflation). In addition to cutting private demand, such wage restraint, when combined with a devaluation and interest rate increases, should help to promote employment through the use of more labor-intensive techniques.

Bank Group Operations

On Thursday, May 11, 1978, the Bank approved its 24th loan to Zambia ($518 million total), but more significantly, its first IDA credit ($11.25 million) for a Third Highway Project ($11.25 million Bank/$11.25 million IDA). The decision to make Zambia eligible for IDA funds is one further indication of the Bank's appreciation of Zambia's problems and our support for their efforts to deal with the situation. We are currently in the process of restructuring our lending operations to focus on agriculture and industry and less on social services and non-essential infrastructure. Our proposed FY79-83 lending program (see Annex 5) contains seven agricultural projects (out of 14 total) for roughly $100 million (out of $259 million total - $205 million Bank and $54 million IDA). A coffee project ($4 million IDA) has been appraised and will be presented in FY79; a cotton project ($10.0 million IDA) is under preparation jointly with the EEC. Other major projects include a proposed Third Program Loan in FY79 ($25 million Bank) and a pulp and paper project ($30 million Bank) for FY80 which the Government has given a high priority.

The IFC, which has several small operations in Zambia totalling $3.9 million, recently appraised a $250 million project to extract copper from accumulated tailings dumps. The project would produce 40,000-50,000 tons of copper per year and would generate substantial revenues and foreign exchange earnings based on current Bank projections of copper prices. The project, however, will require substantial loan capital in view of the limited ability of the Nchanga Consolidated Copper Mines Ltd. to provide the required equity. At issue is the wisdom of Zambia's incurring substantial new external debt on commercial terms for copper production when it is turning to the international community for concessional aid to assist its recovery and its diversification program. While the stress upon diversification is correct, there is also a clear need for investment to maintain (and hopefully add to) copper production to generate foreign exchange and budgetary resources for the development effort and to preserve and improve the country's creditworthiness.

Annex 5

WORLD BANK / INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: Files

DATE: April 20, 1978

FROM: Roger O. Sullivan, Acting Division Chief, EA1DB

SUBJECT: ZAMBIA - Management Review

1. A meeting on March 30, 1978, chaired by Mr. Knapp, reviewed Zambia's economic situation and recent performance, and the Eastern Africa Region's proposed IBRD and IDA lending program, including a third program loan (see Mr. Wiehen's memorandum of March 23 to Mr. Knapp).

2. The meeting agreed that (i) Zambia should continue to be able to borrow on a blend of IBRD/IDA terms; (ii) the $35 million IDA VI allocation for FY81-83, in addition to the $30 million already approved for FY78-80, was satisfactory for the present; (iii) the $300 million of IBRD lending proposed for FY79-83 was too large in view of Zambia's deteriorating economic prospects -- particularly in light of the expected sharp downward revision of copper prices as projected by the Bank's commodity experts; (iv) the region should proceed with preparations for the proposed FY79 program loan; (v) the amount of IBRD and IDA lending for FY79-83 should be reviewed again at the time the loan committee considers the program loan proposal (probably in September/October); and (vi) in the meantime, the proposed IBRD lending should be reduced to $205 million for FY79-83 (as reflected in the revised attachment), with no reduction in the number of projects.

3. Regarding the program loan, it was agreed that one should envisage a loan in two tranches, with disbursement under the second tranche conditional upon the Government's satisfactory performance, as determined by the Bank, against agreed-upon criteria (i.e., the economic action program). The loan would not be linked directly to the IMF standby agreement, but the decisions to proceed with the loan and to present it to the Board would depend upon Zambia's performance under the Fund agreement, and continuing eligibility to draw under the Fund agreement would be a critical factor in judging Zambia's "performance" for second tranche disbursement.

Attachment

Cleared with and cc: Messrs. Horsley, Wiehen, Zaidan

cc: Messrs. Wapenhans, Adler, Acharya, Barry, Bickers, Bronfman, Eccles, Erkmen, Fuchs, Gulhati, Hendry, Jalil, Jordan, McCleary, Nkojo, Nouvel, O'Brien, Pennisi, Reese, Reid, RMEA, Saunders, Strombom, Mrs. Bateman, Ms. Bracher, Ms. Singh

Messrs. Knapp, Baum, Cargill, Gabriel, Goodman, Haq, Karaosmanoglu, Chernick

DGReese/GZaidan:iaj

Attachment I

ZAMBIA - PROPOSED LENDING PROGRAM, FY79-83
(US$ Million)

		FY78	FY79	FY80	FY81	FY82	FY83	FY78-82	FY79-83	Reserve
Agriculture I (Coffee)/TA	IDA		8.75							
Agriculture II (Cotton)	IDA			10.0						
Agriculture III (Western Province)	IDA				10.0					
Agriculture IV	IDA					15.0				
Agriculture V	IBRD						20.0			
Agriculture Unidentified I	IBRD									10.0(FY81)
Agriculture Unidentified II	IBRD									10.0(FY83)
Forestry III	IBRD						*20.0			
Rural Infrastructure	IBRD						20.0			
DFC II/SSE	IBRD					25.0				
Pulp & Paper	IBRD			30.0						
Copper	IBRD									100.0(FY81)
Industry	IBRD									30.0(FY83)
Education V	IBRD				20.0					
Power V	IBRD				*20.0					
Roads III	IBRD/IDA	11.25/11.25								
Roads IV	IBRD					25.0				
Railways	IBRD									25.0(FY82)
Rural Water	IDA				*10.0					
Urban II	IBRD									20.0(FY80)
Program Loan III	IBRD		25.0							
TOTAL	IBRD	11.25	25.0	30.0	40.0	50.0	60.0	156.25	205.0	
	IDA	11.25	8.75	10.0	20.0	15.0	-	65.0	53.75	
		1	2	2	4	3	3	12	14	

* Standby project.